



VIRGINIA BIOTECHNOLOGY RESEARCH PARTNERSHIP AUTHORITY

REPORT ON AUDIT FOR THE YEAR ENDED JUNE 30, 2020

Auditor of Public Accounts
Martha S. Mavredes, CPA
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AUDIT SUMMARY

We have audited the basic financial statements of the Virginia Biotechnology Research Partnership Authority (Authority) as of and for the year ended June 30, 2020, and issued our report thereon, dated December 18, 2020. We were not engaged to audit the financial statements of the Authority's discretely presented component unit, Virginia Biotechnology Research Park Corporation (Corporation); therefore, we did not express an opinion over the discretely presented component unit. Our report, included in the Authority's Annual Report, is available on the Auditor of Public Accounts' website at www.apa.virginia.gov.

Our audit of the Authority for the year ended June 30, 2020, found:

- fair presentation of the financial statements, in all material respects, as it relates to the Authority;
- disclaimer of opinion on the financial statements as it relates to the Corporation;
- no internal control findings requiring management's attention;
- no instances of noncompliance or other matters required to be reported under Government Auditing Standards; and
- one risk alert requiring the attention of management and those charged with governance.

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RISK ALERT

Re-evaluate 8L Capital Project

The Code of Virginia provides the Authority with broad powers to enter into capital projects, employ necessary professionals, and issue related debt in order to fulfill its mission. During the fiscal year, the Authority incurred significant capital outlay expenses related to its \$50 million '8L' capital project (Project). The Authority Board (Board) and its staff have a broad range of relevant expertise and have regularly executed large-scale capital project initiatives since its inception. However, the Authority has often identified unique partnerships or other financing arrangements that have limited its risk. Excluding a 2001 debt issuance that was fully backed by a capital lease with the Commonwealth of Virginia, the Project would result in the Authority's largest debt issuance in its history, requiring annual debt service payments likely to exceed the aggregate of its current annual outflows. As a result, success of the Project is critical to the ongoing financial health of the Authority. We present the following observations of risk for management and the Board to consider in carrying out their operational and fiduciary responsibilities.

In December 2017, the Board established an Exploratory Committee for Expanded Facilities (Facilities Committee) to identify opportunities relating to a new building and parking deck in order to promote innovation and to attract and retain life science and other growth-stage companies in the region. At the March 2018 board meeting, the Facilities Committee recommended to the Board to immediately move forward with a property at 8th and Leigh. At the June 2018 board meeting, the Facilities Committee provided an update on its work and the Board approved its recommendation to use \$100 thousand from capital reserves for an architectural and engineering firm (architect) to begin planning and design for the project. The architect's proposal included \$1.3 million for various services on an estimated \$23.5 million capital project from pre-design through closeout. In February 2019, the Board approved using current resources to fund preliminary stages of the Project with the expectation that it would issue \$25 million in bonds and reimburse itself with proceeds from the debt issuance.

The Facilities Committee indicated at the February board meeting that it would need more authority between board meetings and would check in for approval at designated times; however, no specifics were established regarding the delegation of the Board's authority to the Facilities Committee or management. While the Facilities Committee engaged the Board through numerous collaborative discussions and presentations throughout the process, some contractual decisions did not involve the full Board. Clarity in delegation of authority ensures the will of the governing body is met.

Recommendation 1: The Board may consider more clearly defining the parameters of its delegation of authority to the Facilities Committee and management to procure, or amend, significant construction related contracts.

Upon the Board's approval in May 2019, the Facilities Committee selected a project manager and construction manager through a request for proposal process in July and August, respectively. Management awarded the construction manager a \$3.9 million partial contract in January 2020 to allow the Project to get started with the understanding that additional construction services would be awarded through change orders. The contract included an appendix agreement that authorized approximately \$400 thousand in design services to begin immediately, providing that the Board would issue its decision in writing by March 2020 on whether to fund the rest of the contract. In January 2020, Authority management also increased the contract with the architect by \$900 thousand through informal negotiation, processing approximately \$1.6 million in payments to the architect during fiscal year 2020.

In March 2020, the Board approved the Facilities Committee recommendation to significantly increase the scope of the Project from \$25 million to \$58 million and amended its previous resolution to authorize debt issuance for the new \$58 million amount. At the March meeting, the Board also approved a financial advisor to pursue financing options to move forward with the debt issuance or other arrangements, subject to final Board approval. With the scope increase established, the construction manager submitted a change order request in March to management to increase its contract and scope of services from \$3.9 million to over \$13 million. Management and the Facilities Committee elected not to sign the agreement until financing was assured, though management did approve a change order to increase the construction manager's scope by \$230 thousand in May 2020.

Management and the Facilities Committee appropriately ensured availability of financing prior to committing the Authority to substantial construction services. However, it is also important to recognize that the Project's procurement was structured to be Construction Manager at Risk. This type of procurement is intended to establish one guaranteed maximum price with the construction manager putting the construction manager at risk to deliver the proposed design in its entirety within that price. Establishing any smaller agreements on individual construction phases may unnecessarily shift the risk of cost overruns to the Authority and diminish its leverage in contract negotiations. Our understanding of management's current position as of the date of this report is to establish one guaranteed maximum price for the work remaining once financing is secured, which would be consistent with the objective of this type of procurement.

Recommendation 2: If financing is secured, the Authority should establish one guaranteed maximum price with the construction manager for the full scope of construction services.

In January 2020, a novel coronavirus (COVID-19) was introduced to the United States and, by the end of March, widespread infection and national responses ensued, resulting in a shift for many businesses to working remotely as the nation continues to grapple with the pandemic crisis. Some businesses have begun to re-evaluate their needs for physical space and to build out technology to facilitate remote working on a more long-term basis, which may have long-term effects on commercial real estate projects such as the Authority's Project. Management believes the Project is uniquely equipped to endure these potential market changes since it is designed to meet the needs of bio-

technology companies, including significant convertible lab space, that may continue to be attractive to companies throughout the pandemic. Management asserts that they continue to receive significant interest from prospective customers in need of physical space. As a result, management believes there will be adequate demand for the building.

Nevertheless, significant uncertainty remains. It remains to be seen whether the Authority will be able to procure financing at an acceptable interest rate to allow the Authority to be able to pay its debt service from the projected future revenues of the Project. As of the end of fiscal year 2020, the Authority has spent \$2.8 million of the \$50 million projected total, recently revised down by the Facilities Committee from \$58 million, and signed a contract for approximately an additional \$4 million. If financing is not available or the Board decides not to move forward with the Project, the capital outlay to date would be at risk of impairment. On the other hand, if the Board obtains financing and moves forward as planned, it will be taking on significant investment and debt service during a period of uncertainty.

Recommendation 3: To aid the Board in its decision-making process for the Project, it may consider pursuing a market analysis study taking into account recent market changes prior to accepting up to \$50 million in debt.



Martha S. Mavredes, CPA
Auditor of Public Accounts

Commonwealth of Virginia

Auditor of Public Accounts

P.O. Box 1295
Richmond, Virginia 23218

December 18, 2020

The Honorable Ralph S. Northam
Governor of Virginia

The Honorable Kenneth R. Plum
Chairman, Joint Legislative Audit
And Review Commission

Board Members
Virginia Biotechnology Research Partnership Authority Board
Virginia Biotechnology Research Park Corporation Board

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States, the financial statements of the Virginia Biotechnology Research Partnership Authority (Authority) as of and for the year ended June 30, 2020, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated December 18, 2020. Our report disclaims an opinion on the Authority's discretely presented component unit, Virginia Biotechnology Research Partnership Corporation (Corporation), because we were not engaged to audit the Corporation.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Authority's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

Authority's Response to the Risk Alert

We discussed this report with management at an exit conference held on December 22, 2020. The Authority's response to the risk alert identified in our audit is described in the accompanying section titled "Authority Response." The Authority's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Martha S. Mavredes
AUDITOR OF PUBLIC ACCOUNTS

ZLB/clj

December 22, 2020

Martha Mavredes, CPA
Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218

Dear Martha:

We have reviewed the audit findings and recommendations resulting from the fiscal year 2020 audit by the Auditor of Accounts (APA) and discussed during the exit conference.

The Virginia Biotechnology Partnership Authority acknowledges the audit findings and the following contains management's responses to the concerns and issues raised.

The Virginia Biotechnology Partnership Authority Act (1993, c. 946; 2005, c. 788) lays out the statutory authority of the political subdivision of the Commonwealth – including as it relates to the development of scientific and technological research and development among public and private entities – and promote industrial and economic development, including:

§ 5. Powers of the Authority:

3. Acquire any project and property, real, personal or mixed, tangible or intangible, or any interest therein, by purchase, gift or devise and to sell, lease (whether as lessor or lessee), transfer, convey or dispose of any project or property, real, personal or mixed, tangible or intangible or any interest therein, at any time acquired or held by the Authority on such terms and conditions as may be determined by the Board;
4. Plan, develop, undertake, carry out, construct, equip, improve, rehabilitate, repair, furnish, maintain and operate projects;
9. Employ, in its discretion, consultants, attorneys, architects, engineers, accountants, financial experts, investment bankers, superintendents, managers and such other employees and agents as may be necessary, and to fix their compensation to be payable from funds made available to the Authority.

The Act also provides for the exemption of the Authority from procurement procedures:

§ 15. Exemption of Authority from personnel and procurement procedures.

The provisions of the Virginia Personnel Act (§ 2.2-2900 et seq.) and the Virginia Public Procurement Act (§ 2.2-4300 et seq.) shall not apply to the Authority in the exercise of any power conferred under this Act. (1993, c. 946; 2005, c. 788)

Throughout the 27-year history of the organization, the projects supported within the VA Bio+Tech Park and other localities have each been unique in scope, parties involved, various

VA Bio+Tech Park | 800 E Leigh St. | Richmond, Virginia 23219

financing as well as various ownership. For example, the last significant project Bio+Tech 8 and expansion, was a joint venture with private investors and completed in 2014 – this was a unique financing mechanism and project. No two projects are similar nor are significant projects undertaken every year. In addition, there have been previous projects proposed that the Board chose not to move forward. The expertise of board members, management, as well as relevant consultants and contractors, create the broad-based team to support and advance the project.

Recommendation 1: The Board may consider more clearly defining the parameters of its delegation of authority to the Facilities Committee and management to manage the capital project.

Given our status as an independent authority, typical protocols are not required of Activation Capital. However, management will adopt a communication practice to more clearly document the delegation of authority. This change would include more explicitly phrasing the language of board motions that involve the delegation authority on capital projects.

The authority granted to the Exploratory Committee for Facilities Expansion related to the ongoing capital project called 8L has been well-documented.

Since the Committee's creation, there has been a direct line of communication between the Committee and Board. The Board provides input, approvals, and delegation of authority along the way. While the note by the Auditor of February 2019 action taken by the Board is a moment in time in the prior fiscal year, below is the work of the Committee and Board activity from December 2017 through the end of current audit year FY20 that provides a more robust picture of the process and approvals.

The following account details the decision timeline of approvals for the project:

2017

In December 2017, the Board Chairman, Michael Rao, created the Facilities Expansion Committee to address space needs for existing and new companies, naming the following individuals to the Committee:

- Bob Mooney – also serves as the Finance Committee Chair. He helped establish the Maggie Walker Governor's School, led the College of William & Mary's \$75 million business school building effort as CFO, and led Richmond's \$74 million CenterStage performing-arts complex Executive Director.
- Dr. Eric Edwards - co-founder of Kaleo that started in and graduated from the Bio+Tech Center,
- Jen Finn - corporate sponsor of Capital One's 1717 Innovation Center, and
- Dr. Garret Westlake - Executive Director of VCU DaVinci Center and managed ASU's 1.2 million sq. ft. entrepreneurial center - SkySong

2018

During the March 2018 Board meeting, the Facilities Expansion Committee gave an update and recommendation to the Board. The recommendations were based on a review of existing space needs and a robust gap analysis. Given the capacity challenges, the Committee recommended that the Board approve building additional space.

Among the Committee's next steps included meeting with ecosystem companies and members to understand short- and long-term space constraints/needs. This would drive a decision whether, and to what extent, Activation Capital could assist with broader ecosystem facility needs. The Committee's recommendation to the Board was to immediately move forward with space at 8th and Leigh rather than 4th and Jackson as was done with the past planning for a proposed Bio+Tech 10 building.

At the June 2018 Board meeting, the Facilities Expansion Committee provided an update on their work and a recommendation with the Board approving an initial \$100,000 from capital reserves for SMBW to begin the planning and design of a new building at 8th and Leigh.

In September 2018, Dr. Edwards gave an update on the Facilities Expansion Committee, sharing the project goals developed for the new facility and various stakeholders' engagement in the process.

At the December 2018 Board meeting, Dr. Edwards reminded the Board of the Facilities Expansion Committee's work to this point, including the engagement of SMBW. He noted the Committee has been meeting regularly, and the next steps will include creating a financing plan, using the modeling, and looking at successful spaces around the country. SMBW presented a building massing of what they recommend the size to be based on customer discovery and community stakeholder inputs and guidance on programming and a vision for the Board's building. There was a discussion about the process. Dr. Edwards confirmed the Committee was diligent in following the necessary steps, getting feedback, and engaging the Board appropriately and intentionally.

2019

In January 2019, a group of board members (Bob Mooney, Eric Edwards, and Mary Doswell) and stakeholders (Frank Gupton – head of the VCU Medicines for All Institute located in Bio+Tech 8, Nicky Monk, VCU Ventures) along with Carrie Roth, went to Boston to visit three BioLabs facilities and garner insight on their building design and program model. An executive from BioLabs followed up with a visit to Richmond and reviewed design work for input. Also, research was garnered from the Wexford Chesterfield facility in Durham, which includes a BioLabs space. A debrief of the Boston trip was sent to all members of the Board and Facilities Expansion Committee.

During the February 2019 meeting, the Committee updated the Board on the Boston facilities visit and its financial modeling effort. A request was made for additional funding to continue the work. The Board approved an additional \$1 million from the LGIP assets fund for the continued work on the 8th and Leigh Project (8L). It also approved a resolution for the official intent to reimburse expenditures with proceeds of a borrowing. Following consultation with experienced bond counsel and VRA executive director, this was necessary for the event bonds were the financing mechanism eventually sought by the Authority in the future when the project was ready for financing.

During the March 2019 Board meeting, Carrie Roth addressed upcoming expenses with the 8th and Leigh Project. The Facilities Expansion Committee shared their selection of and work with Facility Logix. This firm provides strategic insight for clients seeking a competitive edge in

growing life science clusters and developing lab and bio-manufacturing spaces. The Committee also gave an update on income projections and the various revenue opportunities to create a pro forma for the building based on their experience with similar projects in life sciences and advanced-technology hubs across the country.

Dr. Edwards shared the group has been thoughtful about every aspect of the building and used the trip to Boston as a reference when considering plans. He noted the consideration of how the locations intake the startup companies and how they work with sponsors, in addition to looking at the actual space. He shared that the Boston trip validated the approach and vision and our intentionality in planning future advanced technologies and life sciences. Dr. Edwards stated Facilities Expansion Committee is engaging the right consultants and making sure whatever we build we can afford, the operational model is sustainable, and the contemplation of the changing landscape in the blocks around us.

A May 2019 Board meeting was called to approve the schematic design for the 8L project. The schematic designs were presented, along with a review of the steps leading up to this point. The Committee indicated that pricing data was forthcoming with the approved modeling and schematic design and when the RFP was sent out to contractors. It was recommended and unanimously approved for the schematics' approval to move forward with the RFP for the construction manager, in addition to hiring a project manager.

In the June 2019 budget presentation to the Board, Ms. Roth noted FY19 was a significant year for Activation Capital with many new projects starting or currently underway, including the 8th and Leigh Project for which an RFP was sent out. The significance this has on the financials is very much understood. She noted good financial stewardship and long-term sustainability planning allow for a temporary decrease in income due to planned construction activities. She concluded her presentation of the FY2020 budget proposal by stating she worked closely with the Finance and Audit Committee members. These projects are getting underway and are being mindful of resources.

During the September 2019 Board meeting, an update on the 8L project noted the pricing was underway.

In December 2019, Dr. Edwards shared an update from the Exploratory Committee for Expanded Facilities. He stated we are creating a one-of-a-kind innovation scale-up hub for life sciences and other advanced technology companies in the region and the Commonwealth. Dr. Edwards shared the excitement for many reasons – most importantly, because it will be a significant economic driver for the Commonwealth focused on the founder. He shared the Committee is highly engaged – meeting monthly and sometimes weekly to get the Authority to the point where we are today – thoughtful and intentional. He said the group focused on place, programs, people, and access to capital throughout the process. SMBW provided an updated building presentation, including a short video of the design. Dr. Edwards reminded the Board of the selection of WMJordan as the construction manager and Ted Tremain with Project Solutions Group as the Project Manager. Once the pricing and model are complete, a presentation will be made to the Board to approve the project's financing. Also, a discussion took place around the role of the City in the project and the impact of sustainability as it relates to the building and the organization.

2020

In the March 2020 Board meeting, Dr. Edwards shared the Finance Committee had a robust discussion regarding the financial needs, pro forma for the building, and selecting the financial advisor. The Committee recommended, and the Authority Board unanimously approved: a revised resolution from February 12, 2019, meeting to capture expenses incurred with the updated project cost of up to \$58 million; Davenport as the financial advisor and give the Authority to move forward with financing; and use of LGIP Operations to help with cash flow for short-term financing until long-term financing is in place.

In the June 2020 fiscal year-end Board meeting, parking revenue was above budget because of the construction delay. That \$1.6 million has been spent on building design, permits, and other preconstruction costs. The Board was also reminded Davenport had been hired as the financial advisor, they had received preliminary interest from several banks and would be sending out a formal RFP.

Recommendation 2: If financing is secured, the Authority should establish one guaranteed maximum price with the construction manager for the full scope of construction services.

Under the Construction Manager at Risk project, the Authority received three sets of estimates: Schematic Design, Design Documents and Construction Documents, all resulting in a reduction of project cost. Following this work, the Authority conducted several rounds of value engineering and finalize the project scope. Once financing is secured, the Authority will establish the guaranteed maximum price with the construction manager.

Recommendation 3: To aid the Board in its decision-making process on the capital project, it may consider pursuing a market analysis study taking into account recent market changes before accepting up to \$50 million in debt.

Given the current market conditions, an updated market analysis is a prudent decision. The Facilities Expansion Committee of the Authority Board met on November 30, 2020, before the December 1, 2020, Authority Board meeting, to discuss a reassessment of the opportunity, including a revised demand forecast. Also, Activation Capital is currently in discussions with real estate experts who are not affiliated with the current project to assess and revise the project's business case.

Activation Capital remains optimistic about demand for capital project – the new 100,000 square-foot "8L" property. Despite the COVID-19 impact on the real estate sector, the life sciences sector continues to experience growth. Activation Capital continues to experience demand for its spaces as established by a growing waitlist for labs in the Bio+Tech Center and additional demand from companies in the Bio+Tech Center preparing for growth. Both factors represent demand beyond what was forecasted in the pro forma originally developed for the 8L project. For example, the existing pro forma was formulated based on needs and pipeline before the announcement of the over \$340 million contract awarded to Phlow Corporation by the federal government – including work supported by the VCU Medicines for All Institute located in Bio+Tech 8 – was announced. This new entity will require additional space for its operations but introduces a co-location model that will attract a pool of pharmaceutical-related companies

seeking to work alongside the Phlow Corporation. Also, a significant amount of work is underway, supported by a GOVA grant, to establish a new industry cluster focused on pharmaceuticals. This state-wide private-public effort has recognized the lack of wet-lab space as a hindrance to this new cluster's establishment and growth, resulting in a significant loss of opportunity for the state. Activation Capital plays a critical role in this effort and has met with and in negotiations with a selection of prospective customers who could lease nearly 90,000 sq.ft. In addition, from July through November 2020, the City of Richmond alone had nearly 388,000 sq.ft. of pipeline activity in the life sciences space.

These recent events enable Activation Capital to remain optimistic about the demand for our planned new property.

Sincerely,

A handwritten signature in black ink that reads "Carrie Roth". The signature is fluid and cursive, with the first name "Carrie" written in a larger, more prominent script than the last name "Roth".

Carrie Roth

VIRGINIA BIOTECHNOLOGY RESEARCH PARTNERSHIP AUTHORITY

As of June 30, 2020

BOARD OF DIRECTORS

Michael Rao, Ex-Officio and Chairman

Mary Doswell, Vice Chairman

Gail Letts, Secretary

Ken Ampy

Eric Edwards

Brian Ball, Ex-Officio

Levar Stoney, Ex-Officio

J. Robert Mooney

Vida Williams

Executive Director

Chandra Briggman

Chief Operating Officer

Carrie Roth

Officers to the Board

Joy Edgett, Treasurer

Sara Maddox, Assistant Secretary to the Board

VIRGINIA BIOTECHNOLOGY RESEARCH PARK CORPORATION

As of June 30, 2020

BOARD OF DIRECTORS

Michael Rao, Ex-Officio and Chair

Jennifer Finn, Vice Chair

John A. Vithoulkas, Ex-Officio and Secretary

Karen Adams

Brian Anderson

Bryan Bostic

Elizabeth Creamer

George Karles

Paul Nolde

Erin Powell

Lisa Sims

Joseph Tannery

Garret Westlake

Ex-Officio

John Budesky

Joseph Casey

P. Srirama Rao

Brian Ball

Levar Stoney

President and CEO

Chandra Briggman

Chief Operating Officer

Carrie Roth

Officers to the Board

Joy Edgett, Treasurer

Sara Maddox, Assistant Secretary to the Board